

Reference Room, 450 Fifth Street, NW., Washington, DC 20549.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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[Release No. 34-35617; File No. SR-CBOE-95-02]

**Self-Regulatory Organizations; Order Approving a Proposed Rule Change by the Chicago Board Options Exchange, Inc., Relating to the Listing of Long-Term Index Options Series ("LEAPS") With a Duration of up to Sixty Months Until Expiration**

April 17, 1995.

On January 19, 1995, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> filed with the Securities and Exchange Commission ("Commission") a proposed rule change to permit the listing of long-term index options series ("LEAPS") with a duration of up to sixty months (five years) until expiration. Notice of the proposal appeared in the **Federal Register** on February 1, 1995.<sup>3</sup> No comment letters were received on the proposed rule change. This order approves the CBOE proposal.

The purpose of the proposed rule change is to permit the Exchange to list index LEAPS with a duration of up to sixty months (five years).<sup>4</sup> Presently, the Exchange has authority pursuant to CBOE Rule 24.9(b) to list index LEAPS that expire from twelve to thirty-six months from the time they are listed. The Exchange represents that there has been increasing member firm and customer interest in longer term instruments. The Exchange, therefore, is proposing to amend Exchange Rule 24.9 to permit the listing of index options with up to sixty months until expiration. In addition, the Exchange proposes to amend Rule 24.9 to allow for up to ten expiration months for index LEAPS, as opposed to the six months currently allowed. The proposal does not change any other rule

regarding the listing and trading of index LEAPS.<sup>5</sup>

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 6(b)(5).<sup>6</sup> Specifically, the Commission believes the proposal is designed to provide investors with additional means of hedging equity portfolios from long-term market risk with an exchange-traded security (*i.e.*, a standardized option), thereby facilitating transactions in options and contributing to the protection of investors and the maintenance of fair and orderly markets.<sup>7</sup>

Currently, institutional customers use index options to hedge the risks associated with holding diversified equity portfolios. The Commission continues to believe, as originally stated in its approval of the listing of index LEAPS by the Exchange, that allowing investors to lock in their hedges with longer-term index LEAPS will permit institutions to protect better their portfolios from adverse market moves.<sup>8</sup> Further, the Commission believes that index LEAPS with up to five years until expiration will allow this protection at a known and limited cost.<sup>9</sup> Moreover, the proposal will provide institutions with an additional securities product with which to hedge their portfolios as an alternative to hedging with futures positions or off-exchange customized index options.<sup>10</sup> Accordingly, the Commission believes that the proposed rule change will better serve the long-term hedging needs of institutional investors.<sup>11</sup>

Finally, although as with index LEAPS presently trading on the Exchange, specific strike price interval, bid/ask differential, and price continuity rules will not apply until the proposed longer-term index LEAPS

<sup>5</sup> See CBOE Rule 24.9(b).

<sup>6</sup> 15 U.S.C. 78f(b)(5) (1988 & Supp. V 1993).

<sup>7</sup> The Commission also finds that extending the maximum term for Index LEAPS from three to five years does not alter the Commission's designation of index LEAPS as standardized options pursuant to Rule 9b-1(a)(4) of the Act.

<sup>8</sup> See Securities Exchange Act Release No. 24853 (August 27, 1987), 52 FR 33486 (September 3, 1987).

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> The Commission's findings are predicated on the somewhat limited length of five-year index LEAPS. Any subsequent proposal to list index LEAPS with expirations beyond five years could alter the nature of the product and would raise new regulatory concerns, including, among other things, the appropriate margin treatment, disclosure, and trading rules for the product.

have less than 12 months until expiration,<sup>12</sup> the Commission notes that CBOE's general rule obligating market makers to maintain fair and orderly markets will continue to apply to the proposed longer-term index LEAPS.<sup>13</sup> The Commission believes that the requirements of CBOE Rule 8.7(a) are broad enough, even in the absence of strike price interval, bid/ask differential, and continuity requirements, to provide the Exchange with the authority to make a finding of inadequate market maker performance should market makers enter into transactions or make bids or offers (or fail to do so) in the proposed longer-term index LEAPS that are inconsistent with the maintenance of a fair and orderly market.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>14</sup> that the proposed rule change (File No. SR-CBOE-95-02) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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[Release No. 34-35614; File No. SR-CHX-95-05]

**Self-Regulatory Organizations; Chicago Stock Exchange, Incorporated; Order Granting Approval to Proposed Rule Change Relating to the Authority of the Committee on Floor Procedure**

April 17, 1995.

On February 10, 1995, the Chicago Stock Exchange, Incorporated ("CHX" or "Exchange") submitted to the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend CHX Rule 3 of Article XII to provide the Committee on Floor Procedure with the same authority over persons associated with a member as it currently has over members. On March 1, 1995, the Exchange submitted to the Commission Amendment No. 1 to the proposed rule change.<sup>3</sup>

<sup>12</sup> See CBOE Rule 24.9(b)(1).

<sup>13</sup> See CBOE Rule 8.7(a).

<sup>14</sup> 15 U.S.C. 78s(b)(2) (1988).

<sup>15</sup> 17 CFR 200.30-3(a)(12) (1994).

<sup>1</sup> 15 U.S.C. 78s(b)(1) (1988).

<sup>2</sup> 17 CFR 240.19b-4 (1994).

<sup>3</sup> See letter from David Rusoff, Foley & Lardner, to Jennifer Choi, SEC, dated February 27, 1995. The original filing incorrectly referenced Rule 3 of Article IV of the Exchange Rules as the rule to be

<sup>11</sup> 17 CFR 200.30-3(a)(16) (1994).

<sup>1</sup> 15 U.S.C. 78s(b)(1) (1988).

<sup>2</sup> 17 CFR 240.19b-4 (1994).

<sup>3</sup> See Securities Exchange Act Release No. 35278 (January 25, 1995), 60 FR 6324.

<sup>4</sup> The proposal would permit five-year LEAPS on both broad-based and narrow-based indexes on which LEAPS have been approved for trading on the CBOE.

The proposed rule change, including Amendment No. 1 thereto, was published for comment in Securities Exchange Act Release No. 35449 (Mar. 7, 1995), 60 FR 13492 (Mar. 13, 1995). No comments were received on the proposal.

At present, Rule 3 of Article XII provides the Committee on Floor Procedure with the authority to summarily fine members and exclude them from the Exchange premises under certain circumstances. The Rule provides that the Committee on Floor Procedure or an appropriately designated subcommittee has the authority to summarily fine and exclude from the Exchange a member whose conduct is deemed to be improper and to recommend investigations pursuant to Rule 1 of Article XII<sup>4</sup> regarding any conduct on the floor of the Exchange. Specifically, any member of the Floor Committee or a member of its appropriately designated subcommittee may summarily fine any member for conduct classified as Class B<sup>5</sup> in an amount not to exceed \$100. For conduct classified as Class A offenses,<sup>6</sup> any member of the Floor Committee or a member of its appropriately designated subcommittee with the concurrence of two other floor officials (floor governors if immediately available) may summarily fine a member in an amount not to exceed \$2,500 and summarily exclude a member from the Exchange for no longer than the remainder of the trading day.

For either class of offenses, a member, who has been adversely affected by any action taken under Rule 3, except for a summary exclusion,<sup>7</sup> by any person or

amended. Amendment No. 1 altered the proposed rule change to reference Rule 3 of Article XII as the correct rule to be amended.

<sup>4</sup> Under Rule 1 of Article XII, any default, misconduct or other offense alleged to have been committed by a member, member organization or any other person or organization subject to the Exchange's jurisdiction that comes to the attention of the president shall be investigated by the staff and a written report of such investigation shall be made to the president. In addition, if the president decides from such a report that such member, member organization, or other person or organization has committed a default or other offense in violation of the Constitution or Rules of the Exchange, the president shall direct the staff to prefer written charges against the accused, a copy of which will be served upon the accused.

<sup>5</sup> Class B violations involve minor offenses such as dress code and smoking violations. See .01 of the Interpretations and Policies to Rule 3 of Article XII.

<sup>6</sup> Class A represents more serious violations than Class B and includes such conduct as fighting, threatening speech, and other conduct that is detrimental to the interest or welfare of the Exchange. See .01 of the Interpretations and Policies to Rule 3 of Article XII.

<sup>7</sup> A member summarily excluded has the right to petition for reinstatement after a sufficient "cooling-off" period has elapsed. See .02 of the Interpretations and Policies to Rule 3 of Article XII.

body, other than the full Floor Procedure Committee, may appeal to the full Floor Procedure Committee within five days of receiving notice of the action by making a written request. Upon appeal, the full Floor Procedure Committee may increase or decrease the amount of a summary fine or the length of an exclusion from the Exchange. The Floor Procedure Committee, however, may not fine a member in an amount in excess of \$2,500 or exclude a member from the Exchange in excess of five full business days. The decision of the Floor Procedure Committee is deemed final with respect to any action involving no more than a \$100 fine.

By written request, a member may appeal a determination of the full Floor Procedure Committee involving more than a \$100 fine to the Executive Committee. The Executive Committee will review the report of the action as certified by the Secretary unless it decides to open the record for additional evidence. Upon review, the Executive Committee may increase or decrease the amount of a summary fine or the length of an exclusion. The Executive Committee, however, may not fine a member in an amount in excess of \$2,500 or exclude a member from the Exchange in excess of five full business days.

The Exchange proposes to amend Rule 3 and interpretation .02 thereunder to extend the application of the rule to persons associated with a member.<sup>8</sup> Therefore, under the proposed rule change, the Committee on Floor Procedure would exercise the same authority over members and persons associated with a member.

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b).<sup>9</sup> The Commission believes the proposal is consistent with the Section 6(b)(6) requirements that the rules of an exchange provide for the appropriate discipline of its members and persons

<sup>8</sup> The Exchange does not specifically define the term "associated person" in its Rules. For purposes of Rule 3, Article XII, the Exchange refers to an associated person as defined in Section 3(a)(21) of the Securities Exchange Act of 1934. Telephone conversation with David Rusoff, Foley & Lardner, and Jennifer Choi, Attorney, SEC, dated February 27, 1995. Section 3(a)(21) defines an "associated person of a member" as any "partner, officer, director, or branch manager of such member (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such member, or any employee of such member."

<sup>9</sup> 15 U.S.C. 78f(b) (1988 & Supp. v 1993).

associated with its members for violation of the Act, the rules promulgated thereunder, or the rules of the exchange because the rule change provides that members and persons associated with a member may be summarily fined or excluded from the Exchange premises for conduct that the Exchange deems improper. Moreover, the Commission believes the proposal is consistent with the Section 6(b)(1) requirements that an exchange have the capacity to enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules promulgated thereunder, and the rules of the exchange because under the proposed rule change, the Exchange's Committee on Floor Procedure would have the authority to enforce compliance by members and persons associated with a member, with the rules that it deems important in the fair administration of the Exchange.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>10</sup> that the proposed rule change (SR-CHX-95-05) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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[Release No. 34-35615; International Series Release No. 802 File No. SR-Phlx-95-05]

### **Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to the Response Period for Customized Foreign Currency Options**

April 17, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on February 21, 1995, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The Phlx proposes to amend Exchange Rule 1069(b) in order to

<sup>10</sup> 15 U.S.C. 78s(b)(2) (1988).

<sup>11</sup> 17 CFR 200.30-3(a)(12) (1994).